

of a facility or facilities are not exempt function income. For the purposes of section 528, dues, fees, or assessments which are based on the assessed value or size of property will be considered as arising solely as a result of membership in the organization. Regardless of the organization's method of accounting, excess assessments during a taxable year which are either rebated to the members or applied to their future assessments are not considered gross income and therefore will not be considered exempt function income for such taxable year. However, if such excess assessments are applied to a future year's assessments, they will be considered gross income and exempt function income for that future year. In addition, assessments in a taxable year, such as an assessment for a capital improvement, which are not treated as gross income do not enter into the determination of whether the organization meets the source of income test for that taxable year.

(b) *Examples of exempt function income.* Assessments which are considered more in the nature of a fee for common activity than for the providing of services and which will therefore generally be considered exempt function income include assessments made for the purpose of:

- (1) Paying the principal and interest on debts incurred for the acquisition of association property;
- (2) Paying real estate taxes on association property;
- (3) Maintaining association property;
- (4) Removing snow from public areas; and
- (5) Removing trash.

(c) *Examples of receipts which are not exempt function income.* Exempt function income does not include:

- (1) Amounts which are not includible in the organization's gross income other than by reason of section 528 (for example, tax-exempt interest);
- (2) Amounts received from persons who are not members of the association;
- (3) Amounts received from members for special use of the organization's facilities, the use of which is not available to all members as a result of having paid the dues, fees or assessments required to be paid by all members;

(4) Interest earned on amounts set aside in a sinking fund;

(5) Amounts received for work done on privately owned property which is not association property; or

(6) Amounts received from members in return for their transportation to or from shopping areas, work location, etc.

(d) *Special rule.* Notwithstanding paragraphs (a) and (c)(3) of this section, amounts received from members or tenants of residential units owned by members (notwithstanding § 1.528-1(d)) for special use of an association's facilities will be considered exempt function income if:

(1) The amounts paid by the members are not paid more than once in any 12 month period; and

(2) The privilege obtained from the payment of such amounts lasts for the entire 12 month period or portion thereof in which the facility is commonly in use.

Thus, amounts received as the result of payments by members of a yearly fee for use of tennis courts or a swimming pool shall be considered exempt function income. However, amounts received for the use of a building for an evening, weekend, week, etc., shall not be considered exempt function income.

[T.D. 7692, 45 FR 26323, Apr. 18, 1980]

§ 1.528-10 Special rules for computation of homeowners association taxable income and tax.

(a) *In general.* Homeowners association taxable income shall be determined according to the provisions of section 528(d) and the rules set forth in this section.

(b) *Limitation on capital losses.* If for any taxable year a homeowners association has a net capital loss, the rules of sections 1211(a) and 1212(a) shall apply.

(c) *Allowable deductions*—(1) *In general.* To be deductible in computing the unrelated business taxable income of a homeowners association, expenses, depreciation and similar items must not only qualify as items of deduction allowed by chapter 1 of the Code but must also be directly connected with the production of gross income (excluding exempt function income). To be *directly connected with* the production of

gross income (excluding exempt function income), an item of deduction must have both proximate and primary relationship to the production of such income and have been incurred in the production of such income. Items of deduction attributable solely to items of gross income (excluding exempt function income) are proximately and primarily related to such income. Whether an item of deduction is incurred in the production of gross income (excluding exempt function income) is determined on the basis of all the facts and circumstances involved in each case.

(2) *Dual use of facilities or personnel.* Where facilities are used both for exempt functions of the organization and for the production of gross income (excluding exempt function income), expenses, depreciation and similar items attributable to such facilities (for example, items of overhead) shall be allocated between the two uses on a reasonable basis. Similarly where personnel are employed both for exempt functions and for the production of gross income (excluding exempt function income), expenses and similar items attributable to such personnel (for example, items of salary) shall be allocated between the two activities on a reasonable basis. The portion of any such item so allocated to the production of gross income (excluding exempt function income) is directly connected with such income and shall be allowable as a deduction in computing homeowners association taxable income to the extent that it qualifies as an item of deduction allowed by chapter 1 of the Code. Thus, for example, assume that X, a homeowners association, pays its manager a salary of \$10,000 a year and that it derives gross income other than exempt function income. If 10 percent of the manager's time during the year is devoted to deriving X's gross income (other than exempt function income), a deduction of \$1,000 (10 percent of \$10,000) would generally be allowable for purposes of computing X's homeowners association taxable income.

(d) *Investment credit.* A homeowners association is not entitled to an investment credit.

(e) *Cross reference.* For the definition of exempt function income, see § 1.528-9.

[T.D. 7692, 45 FR 26324, Apr. 18, 1980]

CORPORATIONS USED TO AVOID INCOME TAX ON SHAREHOLDERS

CORPORATIONS IMPROPERLY ACCUMULATING SURPLUS

§ 1.531-1 Imposition of tax.

Section 531 imposes (in addition to the other taxes imposed upon corporations by chapter 1 of the Code) a graduated tax on the accumulated taxable income of every corporation described in section 532 and § 1.532-1. In the case of an affiliated group which makes or is required to make a consolidated return see § 1.1502-43. All of the taxes on corporations under chapter 1 of the Code are treated as one tax for purposes of assessment, collection, payment, period of limitations, etc. See section 535 and §§ 1.535-1, 1.535-2, and 1.535-3 for the definition and determination of accumulated taxable income.

(Secs. 1502 and 7805 of the Internal Revenue Code of 1954 (68A Stat. 637, 917; 26 U.S.C. 1502, 7805))

[T.D. 6500, 25 FR 11737, Nov. 26, 1960, as amended by T.D. 7244, 37 FR 28897, Dec. 30, 1972; T.D. 7937, 49 FR 3462, Jan. 27, 1984]

§ 1.532-1 Corporations subject to accumulated earnings tax.

(a) *General rule.* (1) The tax imposed by section 531 applies to any domestic or foreign corporation (not specifically excepted under section 532(b) and paragraph (b) of this section) formed or availed of to avoid or prevent the imposition of the individual income tax on its shareholders, or on the shareholders of any other corporation, by permitting earnings and profits to accumulate instead of dividing or distributing them. See section 533 and § 1.533-1, relating to evidence of purpose to avoid income tax with respect to shareholders.

(2) The tax imposed by section 531 may apply if the avoidance is accomplished through the formation or use of one corporation or a chain of corporations. For example, if the capital stock of the M Corporation is held by the N